



The Accounting Officer  
Govan Mbeki Local Municipality  
Private Bag X1017  
Secunda  
2302

30 November 2017

Reference: 03014REG16-17

Dear Sir

**Report of the Auditor-General on the financial statements and other legal and regulatory requirements of Govan Mbeki Municipality for the year ended 30 June 2017**

1. The above-mentioned report of the Auditor-General is submitted herewith in terms of section 21(1) of the Public Audit Act of South Africa read in conjunction with section 188 of the Constitution of the Republic of South Africa section 121(3) of the Municipal Finance Management Act of South Africa (MFMA).
2. In terms of section 121(3) of the MFMA you are required to include the audit report in the municipality's annual report to be tabled.
3. Until the annual report is tabled as required by section 127(2) of the MFMA the audit report is not a public document and should therefore be treated as confidential.
4. Prior to printing or copying the annual report which will include the audit report you are required to do the following:
  - Submit the final printer's proof of the annual report to the relevant senior manager of the Auditor-General of South Africa for verification of the audit-related references in the audit report and for confirmation that the financial statements and other information are those documents that have been read and audited. Special care should be taken with the page references in your report, since an incorrect reference could have audit implications.
  - The signature *Auditor-General* in the handwriting of the auditor authorised to sign the audit report at the end of the hard copy of the audit report should be scanned in when preparing to print the report. This signature, as well as the place and date of signing and the Auditor-General of South Africa's logo, should appear at the end of the report, as in the hard copy that is provided to you. The official logo will be made available to you in electronic format.
5. Please notify the undersigned Business Executive well in advance of the date on which the annual report containing this audit report will be tabled.
6. Your cooperation to ensure that all these requirements are met would be much appreciated.

Kindly acknowledge receipt of this letter.

Yours sincerely

Signed

A handwritten signature in black ink, appearing to read "Nkosana Zondi". It is written in a cursive style with a dotted line underneath for placement.

Senior Manager: Mpumalanga

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# **Report of the auditor-general to the Mpumalanga Provincial Legislature and the council on the Govan Mbeki Municipality**

## **Report on the audit of the financial statements**

### **Opinion**

1. I have audited the financial statements of the Govan Mbeki Municipality set out on pages ... to ..., which comprise the appropriation statement, the statement of financial position as at 30 June 2017, the statement of financial performance, statement of changes in net assets, cash flow statement and statement of comparison of budget information with actual information for the year then ended, as well as the notes to the financial statements, including a summary of significant accounting policies.
2. In my opinion, the financial statements present fairly, in all material respects, the financial position of the Govan Mbeki Municipality as at 30 June 2017, and its financial performance and cash flows for the year then ended in accordance with the South African Standards of Generally Recognised Accounting Practice (SA Standards of GRAP) and the requirements of the Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMA) and the Division of Revenue Act of South Africa, 2016 (Act No. 3 of 2016) (DoRA).

### **Basis for opinion**

3. I conducted my audit in accordance with the International Standards on Auditing (ISAs). My responsibilities under those standards are further described in the auditor-general's responsibilities for the audit of the financial statements section of my report.
4. I am independent of the municipality in accordance with the International Ethics Standards Board for Accountants' *Code of ethics for professional accountants* (IESBA code) together with the ethical requirements that are relevant to my audit in South Africa. I have fulfilled my other ethical responsibilities in accordance with these requirements and the IESBA code.
5. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my opinion.

### **Emphasis of matters**

6. I draw attention to the matters below. My opinion is not modified in respect of these matters.

### **Restatement of corresponding figures**

7. As disclosed in note 49 to the financial statements, the corresponding figures for 30 June 2016 have been restated as a result of an error in the financial statements of the municipality at, and for the year ended, 30 June 2017.

## **Subsequent events**

8. As disclosed in note 53 of the financial statements, material items were written off by the council subsequent to year-end, which resulted in subsequent adjustments being made to the financial statements for the year ended 30 June 2017.

## **Material impairments – trade debtors**

9. As disclosed in note 38 to the financial statements, material losses to the amount of R227 097 345 were incurred as a result of the provision for irrecoverable trade debtors.

## **Material losses – water**

10. As disclosed in note 57 to the financial statements, material water losses to the amount of R86 744 740 (2015-16: R70 844 910) were incurred, which represented 32% (2015-16: 25%) of the total water purchased. Technical losses amounted to R27 232 597 (2015-16: R28 493 445) and were due to poor infrastructure. Non-technical losses amounted to R59 533 845 (2015-16: R42 351 464) and were due to the poor repair and maintenance of infrastructure.

## **Material losses – electricity**

11. As disclosed in note 57 to the financial statements, material electricity losses to the amount of R168 580 752 (2015-16: R151 476 572) were incurred, which represented 48% (2015-16: 45%) of the total electricity purchased. Technical losses amounted to R35 382 622 (2015-16: R33 709 614) and were due to aging infrastructure. Non-technical losses amounted to R133 191 130 (2015-16: R117 766 957) and were due to the poor monitoring of illegal connections.

## **Unauthorised expenditure**

12. As disclosed in note 54 to the financial statements, unauthorised expenditure of R311 174 006 was incurred, due to the overspending of votes.

## **Irregular expenditure**

13. As disclosed in note 56 to the financial statements, irregular expenditure of R272 274 068 was incurred, as proper tender processes had not been followed.

## **Fruitless and wasteful expenditure**

14. As disclosed in note 55 to the financial statements, fruitless and wasteful expenditure of R63 359 943 was incurred, as interest was charged on overdue accounts.

## **Other matter**

15. I draw attention to the matter below. My opinion is not modified in respect of this matter.

## **Unaudited disclosure notes**

16. In terms of section 125(2)(e) of the MFMA, the municipality is required to disclose particulars of non-compliance with the MFMA in the financial statements. This disclosure requirement did not form part of the audit of the financial statements and, accordingly, I do not express an opinion thereon.

## **Responsibilities of the accounting officer**

17. The accounting officer is responsible for the preparation and fair presentation of the financial statements in accordance with the SA Standards of GRAP and the requirements of the MFMA and DoRA, and for such internal control as the accounting officer determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.
18. In preparing the financial statements, the accounting officer is responsible for assessing the municipality's ability to continue as a going concern, disclosing, as applicable, matters relating to going concern and using the going concern basis of accounting unless the accounting officer either intends to liquidate the municipality or to cease operations, or has no realistic alternative but to do so.

## **Auditor-general's responsibilities for the audit of the financial statements**

19. My objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes my opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with the ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.
20. A further description of my responsibilities for the audit of the financial statements is included in the annexure to the auditor's report.

### **Report on the audit of the annual performance report**

#### **Introduction and scope**

21. In accordance with the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA) and the general notice issued in terms thereof, I have a responsibility to report material findings on the reported performance information against predetermined objectives for selected programmes presented in the annual performance report. I performed procedures to identify findings but not to gather evidence to express assurance.

22. My procedures address the reported performance information, which must be based on the approved performance planning documents of the municipality. I have not evaluated the completeness and appropriateness of the performance indicators/measures included in the planning documents. My procedures also did not extend to any disclosures or assertions relating to planned performance strategies and information in respect of future periods that may be included as part of the reported performance information. Accordingly, my findings do not extend to these matters.

23. I evaluated the usefulness and reliability of the reported performance information in accordance with the criteria developed from the performance management and reporting framework, as defined in the general notice, for the following selected programmes presented in the annual performance report of the municipality for the year ended 30 June 2017:

| Programmes                                | Pages in the annual performance report |
|---|--|
| KPA 2: physical infrastructure and energy | x – x                                  |
| KPA 3: services and customer care         | x – x                                  |

24. I performed procedures to determine whether the reported performance information was properly presented and whether performance was consistent with the approved performance planning documents. I performed further procedures to determine whether the indicators and related targets were measurable and relevant, and assessed the reliability of the reported performance information to determine whether it was valid, accurate and complete.

25. The material findings in respect of the usefulness and reliability of the selected programmes are as follows:

### **KPA 2: physical infrastructure and energy**

#### Percentage compliance to quality of effluent water

26. I was unable to obtain sufficient appropriate evidence for the 50,2% compliance to quality of effluent water by June 2017 that clearly defined the predetermined method of calculation, as required by the Framework for Managing Programme Performance Information (FMPPI). This was due to management not being able to provide sufficient information and computerised formulas having to be used to re-calculate the reported information. I was unable to test whether the target for this indicator was clearly defined by alternative means.

#### Percentage compliance with SANS 241

27. I was unable to obtain sufficient appropriate evidence for the 98,9% water compliance with SANS 241 by June 2017 that clearly defined the predetermined method of calculation, as required by the FMPPI. This was due to management not being able to provide sufficient information and computerised formulas having to be used to re-calculate the reported information. I was unable to test whether the target for this indicator was clearly defined by alternative means.

## **KPA 3: services and customer care**

Number of households to be provided with access to basic electricity

28. I was unable to obtain sufficient appropriate evidence for the reported achievement of the target. This was due to limitations placed on the scope of my work. I was unable to confirm the reported performance through alternative means. Consequently, I was unable to determine whether any adjustments were required to the reported performance of 111 households provided with access to basic electricity.

Number of households receiving a weekly refuse removal service

29. I was unable to obtain sufficient appropriate evidence for the reported achievement of the target. This was due to limitations placed on the scope of my work. I was unable to confirm the reported performance through alternative means. Consequently, I was unable to determine whether any adjustments were required to the reported performance of 83 874 households receiving a weekly refuse removal service.

## **Other matters**

30. I draw attention to the matters below.

Achievement of planned targets

31. Refer to the annual performance report on pages ... to ... and ... to ... for information on the achievement of planned targets for the year and explanations provided for the under- or overachievement of a significant number of targets. This information should be considered in the context of the material findings on the reliability of the reported performance information in paragraphs 26 to 29 of this report.

Adjustment of material misstatements

32. I identified material misstatements in the annual performance report submitted for auditing. These material misstatements were on the reported performance information of length of roads rehabilitated and maintained, length of roads maintained, number of indigent households with access to basic services, and number of households with access to basic electricity. As management subsequently corrected only some of the misstatements, I raised material findings on the usefulness and reliability of the reported performance information. Those that were not corrected are reported above.

## **Report on the audit of compliance with legislation**

### **Introduction and scope**

33. In accordance with the PAA and the general notice issued in terms thereof, I have a responsibility to report material findings on the compliance of the municipality with specific matters in key legislation. I performed procedures to identify findings but not to gather evidence to express assurance.

## Consequence management

34. Unauthorised expenditure incurred by the municipality was not investigated to determine if any person was liable for the expenditure, as required by section 32(2)(a) of the MFMA.
35. Irregular expenditure incurred by the municipality was not investigated to determine if any person was liable for the expenditure, as required by section 32(2)(b) of the MFMA.
36. Some of the fruitless and wasteful expenditure incurred by the municipality was not investigated to determine if any person was liable for the expenditure, as required by section 32(2)(b) of the MFMA.
37. Terms of reference were not always approved by the council for the investigation of financial misconduct, as required by municipal regulation on financial misconduct procedures and criminal proceedings 6(1).
38. Cases of financial misconduct that constitutes a crime committed by officials were not always reported to the South African Police Service, as required by municipal regulation on financial misconduct procedures and criminal proceedings 10(1).

## Annual financial statements

39. The financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122 of the MFMA. Material misstatements of non-current assets and disclosure items identified by the auditors in the submitted financial statements were subsequently corrected and the supporting records provided, resulting in the financial statements receiving an unqualified audit opinion.

## Budgets

40. Reasonable steps were not taken to prevent unauthorised expenditure amounting to R311 174 006, as disclosed in note 54 to the annual financial statements, in contravention of section 62(1)(d) of the MFMA. The majority of the unauthorised expenditure was caused by the overspending of a vote.

## Expenditure management

41. Money owed by the municipality was not always paid within 30 days, as required by section 65(2)(e) of the MFMA.
42. Effective steps were not taken to prevent irregular expenditure amounting to R272 274 068, as disclosed in note 56 to the annual financial statements, as required by section 62(1)(d) of the MFMA. The majority of the irregular expenditure was caused by services rendered without a contract and services received on expired contracts.
43. Effective steps were not taken to prevent fruitless and wasteful expenditure amounting to R63 359 943, as disclosed in note 55 to the annual financial statements, in contravention of section 62(1)(d) of the MFMA. The majority of the disclosed fruitless and wasteful expenditure was caused by late payments on Eskom accounts due to cash-flow problems. Fruitless and wasteful expenditure amounting to R31 172 196 was incurred on Eskom accounts.

## Procurement and contract management

44. Sufficient appropriate audit evidence could not be obtained that contracts had been awarded to only bidders who submitted a declaration on whether they were employed by the state or connected to any person employed by the state, as required by supply chain management (SCM) regulation 13(c).
45. Some quotations were accepted from bidders who did not submit a declaration on whether they are employed by the state or connected to any person employed by the state, as required by SCM regulation 13(c).
46. Some invitations for competitive bidding were not advertised for the required minimum period, in contravention of SCM regulation 22(1) and 22(2).
47. Some contracts were awarded to bidders based on points given for criteria that differed from those stipulated in the original invitation for bidding and quotations, in contravention of SCM regulations 21(b) and 28(1)(a) and the Preferential Procurement Regulations.
48. Some competitive bids were adjudicated by a bid adjudication committee that was not composed in accordance with SCM regulation 29(2).
49. Some contracts were made to bidders other than those recommended by the bid evaluation committee without ratification by the accounting officer, as required by SCM regulation 29(5)(b).
50. The preference point system was not applied in some of the procurement of goods and services above R30 000, as required by section 2(a) of the Preferential Procurement Policy Framework Act of South Africa, 2000 (Act No. 5 of 2000) (PPPFA) and treasury regulation 16A6.3(b).
51. Some quotations were awarded to bidders based on preference points that were not allocated and calculated in accordance with the requirements of the PPPFA and its regulations. Similar non-compliance was also reported in the prior year.
52. Some quotations were awarded to bidders that did not score the highest points in the evaluation process, as required by section 2(1)(f) of the PPPFA and the Preferential Procurement Regulations.
53. Sufficient appropriate audit evidence could not be obtained that construction contracts had been awarded to only contractors that were registered with the Construction Industry Development Board (CIDB) and qualified for the contract in accordance with section 18(1) of the CIDB Act of South Africa, 2000 (Act No. 38 of 2000) and CIDB regulations 17 and 25(7A). Similar non-compliance was also reported in the prior year.
54. Bid documentation for the procurement of commodities designated for local content and production did not stipulate the minimum threshold for local production and content, as required by preferential procurement regulation 9(1).
55. Awards were made to a provider who was in the service of the municipality, in contravention of section 112(j) of the MFMA and SCM regulation 44. Furthermore, the provider failed to declare that he was in the service of the municipality, as required by SCM regulation 13(c).

56. Awards were made to providers who were in the service of other state institutions or whose directors were in the service of the municipality, in contravention of section 112(j) of the MFMA and SCM regulation 44.
57. Persons in the service of the municipality whose close family members had a private or business interest in contracts awarded by the municipality failed to disclose such interest, in contravention of SCM regulation 46(2)(e) and the code of conduct for staff members issued in terms of the Municipal Systems Act of South Africa, 2000 (Act No. 32 of 2000).
58. Some commodities designated for local content and production were procured from suppliers who did not submit a declaration on local production and content, as required by preferential procurement regulation 9(1).
59. Some commodities designated for local content and production were procured from suppliers who did not meet the prescribed minimum threshold for local production and content, as required by preferential procurement regulation 9(5). Similar non-compliance was also reported in the prior year.
60. The performance of some contractors was not monitored on a monthly basis, as required by section 116(2)(b) of the MFMA.
61. Contract performance and monitoring measures and methods were insufficient to ensure effective contract management, in contravention of section 116(2)(c) of the MFMA.

#### **Other information**

62. The municipality's accounting officer is responsible for the other information. The other information comprises the information included in the annual report. The other information does not include the financial statements, the auditor's report thereon and those selected programmes presented in the annual performance report that have been specifically reported on in the auditor's report.
63. My opinion on the financial statements and findings on the reported performance information and compliance with legislation do not cover the other information and I do not express an audit opinion or any form of assurance conclusion thereon.
64. In connection with my audit, my responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements and the selected programmes presented in the annual performance report, or my knowledge obtained in the audit, or otherwise appears to be materially misstated. If, based on the work I have performed on the other information obtained prior to the date of this auditor's report, I conclude that there is a material misstatement of this other information, I am required to report that fact.
65. I have read the other information included in the draft annual report and have nothing to report in this regard.

66. I have not yet received the final annual report containing the other information. When I do receive this information, and if I conclude that it contains a material misstatement, I am required to communicate the matter to those charged with governance and to request the other information to be corrected. If the other information is not corrected, I may have to re-issue my auditor's report amended as appropriate.

### **Internal control deficiencies**

67. I considered internal control relevant to my audit of the financial statements, reported performance information and compliance with applicable legislation; however, my objective was not to express any form of assurance thereon. The matters reported below are limited to the significant internal control deficiencies that resulted in the findings on the annual performance report and the findings on compliance with legislation included in this report.

#### **Financial and performance management**

68. Adequate monitoring processes were not in place to prevent non-compliance and findings on performance management reports.

69. Management did not ensure that there are proper review processes to prevent and/or identify material misstatements in the financial statements.

*Auditor - General*

Mbombela

30 November 2017



*Auditing to build public confidence*

## **Annexure – Auditor-general’s responsibility for the audit**

1. As part of an audit in accordance with the ISAs, I exercise professional judgement and maintain professional scepticism throughout my audit of the financial statements, and the procedures performed on reported performance information for selected programmes and on the municipality's compliance with respect to the selected subject matters.

### **Financial statements**

2. In addition to my responsibility for the audit of the financial statements as described in the auditor's report, I also:
  - identify and assess the risks of material misstatement of the financial statements whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for my opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
  - obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the municipality's internal control.
  - evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the accounting officer.
  - conclude on the appropriateness of the accounting officer's use of the going concern basis of accounting in the preparation of the financial statements. I also conclude, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the municipality's ability to continue as a going concern. If I conclude that a material uncertainty exists, I am required to draw attention in my auditor's report to the related disclosures in the financial statements about the material uncertainty or, if such disclosures are inadequate, to modify the opinion on the financial statements. My conclusions are based on the information available to me at the date of the auditor's report. However, future events or conditions may cause the municipality to cease to continue as a going concern.
  - evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

### **Communication with those charged with governance**

3. I communicate with the accounting officer regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that I identify during my audit.
4. I also confirm to the accounting officer that I have complied with relevant ethical requirements regarding independence, and communicate all relationships and other matters that may reasonably be thought to have a bearing on my independence and, where applicable, related safeguards.